

What factors should Medicare take into account in setting payment rates?

ISSUE: In assessing Medicare's payment policies, commissioners and policymakers often have to decide whether and how they should take into account factors that are unrelated to providers' unit costs for serving beneficiaries. Examples include geographic disparities in Medicare+Choice payment rates, hospitals' uncompensated care burdens, and state Medicaid programs' low payment rates for nursing home care.

KEY POINTS: This paper is intended to stimulate commissioners' discussion of the role such factors should play in influencing Medicare's payment rates for products and services furnished to beneficiaries. In it we argue that these factors have two common characteristics. They reflect additional objectives beyond simply ensuring beneficiaries' access to high quality care in each market and they are largely or completely unrelated to providers' unit costs for serving Medicare patients. The logic of MedPAC's payment policy framework suggests that to ensure beneficiaries' access to high quality care in each market, Medicare's payment rates must approximate efficient providers' marginal costs. Departures from that standard may entail substantial problems for beneficiaries or taxpayers. Consequently, attempting to achieve secondary objectives—preserving access to care for low-income uninsured people, for instance—through Medicare's payment rates may entail substantial costs in the form of providers' undesirable responses to distorted payment rates. It is also important to ask whether secondary objectives pursued through Medicare's payment rates are accomplished. The paper argues that success requires well-defined objectives. But effectiveness also depends on whether the related payment adjustments are tied directly to the intended provider behaviors.

ACTION: No action is required on this topic at this meeting. Unless you determine otherwise, we do not intend to include this topic in this year's March or June reports to the Congress. Commissioners should discuss whether, how, and when you might want to take on some of these issues.

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